MINUTES
of the
SIXTH MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

December 17-18, 2013
Room 307, State Capitol
Santa Fe

The sixth meeting of the Revenue Stabilization and Tax Policy Committee (RSTP) was called to order by Senator Carlos R. Cisneros, chair, on Tuesday, December 17, 2013, at 10:10 a.m. in Room 307 of the State Capitol in Santa Fe.

Present
Sen. Carlos R. Cisneros, Chair
Rep. Edward C. Sandoval, Vice Chair
Sen. Sue Wilson Beffort
Rep. Anna M. Crook
Rep. Brian F. Egolf, Jr.
Sen. Timothy M. Keller (12/18)
Rep. Rodolpho "Rudy" S. Martinez
Sen. Mark Moores
Sen. Clemente Sanchez
Sen. William E. Sharer
Sen. John Arthur Smith
Rep. James R.J. Strickler
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo
Sen. Peter Wirth
Rep. Bob Wooley

Absent
Rep. Henry Kiki Saavedra
Sen. Lisa A. Torraco

Designees
Rep. Ernest H. Chavez (attending as a guest 12/17)
Rep. Jason C. Harper (attending as a designee 12/17 and as a guest 12/18)
Rep. Sandra D. Jeff (attending as a guest 12/17)
Rep. Bill McCamley (attending as a guest 12/18)
Rep. Debbie A. Rodella (attending as a guest 12/18)
Sen. Nancy Rodriguez (12/17)

Rep. Donald E. Bratton
Sen. William F. Burt
Sen. Jacob R. Candelaria
Rep. Miguel P. Garcia
Sen. Phil A. Griego
Sen. Gay G. Kernan
Rep. Tim D. Lewis
Sen. George K. Munoz
Rep. Paul A. Pacheco
Rep. Dennis J. Roch
Sen. John M. Sapien
Sen. Pat Woods

Rep. Carl Trujillo (attending as a guest
12/17)
Rep. Luciano "Lucky" Varela

Guest Legislator
Rep. Roberto "Bobby" J. Gonzales

(Attendance dates are noted for members not present for the entire meeting.)

Staff
Pam Stokes, Staff Attorney, Legislative Council Service (LCS)
Amy Chavez-Romero, Assistant Director for Drafting Services, LCS
Tessa Ryan, Staff Attorney, LCS
Jennifer Dana, Intern, LCS

Guests
The guest list is in the meeting file.

Handouts
Handouts and other written testimony are in the meeting file.

<u>**Tuesday, December 17**</u>

Approval of Minutes
Upon a motion made and seconded, the minutes of the October meeting were approved.

Revenue Forecast
Leila Burrows, chief economist, Department of Finance and Administration, Peter B. van Moorsel, chief economist, Legislative Finance Committee (LFC), and Elisa Walker-Moran, chief economist, Taxation and Revenue Department (TRD), spoke about the consensus revenue estimating group's December 2013 consensus revenue estimate.

Mr. van Moorsel, referring to a handout distributed to the committee, summarized the group's major findings and revisions to the revenue outlook. He remarked that gridlock in Congress, federal sequestration and changes in energy prices have affected, and are predicted to continue affecting, revenue generation.

Ms. Walker-Moran and Ms. Burrows, referring to a separate handout distributed to the committee, expanded on Mr. van Moorsel's commentary. Ms. Walker-Moran reviewed some trends in gross receipts tax revenues, particularly those driven by the phase-out of hold harmless payments, federal budget austerity, payroll tax cuts, the spike in high-wage jobs tax credit claims, the rollout of the new federal health law, changes in personal and corporate income tax collection levels and changes in oil and gas production and prices. Ms. Burrows highlighted some forecast risks and gave an update of the general fund's status and details of the fund's reserves. She also spoke briefly about the estimated authorized bonding capacity.

Committee members' questions and comments and the presenters' responses to them are summarized as follows.

- Will oil production increases in Mexico and other foreign countries drive down oil prices, thereby decreasing state revenues? Ms. Burrows speculated that such foreign activity would reduce the price, but likely not dramatically.
- Why is revenue from the "Professional, Scientific and Technical Services" category trending low? Ms. Walker-Moran responded that the indicator reflects a decline in federal contract spending.
- Would Congress' reaching a budget deal improve economic indicators? Mr. van Moorsel prefaced his answer by saying that forecast data were compiled before the deal was proposed, and so the prospect of its realization was not considered when the forecast was developed. He answered that the deal, if made, would likely increase revenue generation.
- With general fund reserves at between 9% and 10% of the budget — about $500 million — and evidence of recovery, a state the size of New Mexico could consider tapping some of its savings for use by the private or public sector. Mr. van Moorsel explained that the official target for reserves is set at around 10% because the state is so heavily dependent on volatile revenue sources. David Abbey, director, LFC, who was in the audience, articulated more reasons that the state should aim for that approximate level of reserves.
- What explains the increases in gross receipts tax revenue from the manufacturing and construction sectors? Ms. Burrows said that part of the increase in revenue from the manufacturing sector results from a tax-liability shift to utility companies. Ms. Walker-Moran attributed the increase in construction-sector revenue in part to that sector's post-downturn recovery.
- Are protests of denials of high-wage jobs tax credit claims likely? Ms. Walker-Moran said that the TRD is in the process of reviewing claims, that many claims are being denied and that protests will likely follow.

Attorney General Opinion No. 13-03: May the Governor Unilaterally Withhold a Capital Outlay Appropriation Made to an Agency by the Legislature?

Albert J. Lama, chief deputy attorney general, reviewed a recently issued attorney general opinion on the question of whether the governor may unilaterally withhold a capital outlay appropriation made to an agency by the legislature. Copies of the opinion were distributed to the committee.

Mr. Lama summarized the legal precedent relevant to the question and the reasoning that formed the basis of the conclusion, which is that the governor violated the separation of powers doctrine by withholding capital outlay appropriations that were properly appropriated by the legislature. In response to questions by committee members, Mr. Lama remarked that the issue: 1) could likely be pursued in court if certain requirements were met; and 2) did not involve the question of a governor's authority to veto an appropriation. Members commented that: 1) rather than attempting to bind agencies after appropriations were made, the governor could have vetoed projects and stayed within her authority; 2) project-related audits are worthwhile, and legislators who request funding for particular capital outlay projects should investigate whether appropriate audits have been performed and have yielded positive findings; and 3) this request for and the rendering of an opinion might have the unintended consequence of provoking the governor to veto more appropriations in the next cycle. In response to a question, Pam Ray, contract worker, LCS, said that she believed that the new capital outlay form will have a question asking whether audits for a recipient agency are current. In closing, Mr. Lama commented that the legislature could, if it wished, incorporate terms of the executive order into either a particular appropriation or, by passing an all-encompassing law, all future capital outlay appropriations.

Retiree Program Solvency Report

Wayne Propst, executive director, Public Employees Retirement Association (PERA), gave a presentation on the status of the public employee retirement program, information on which was contained in a handout and distributed to the committee.

Mr. Propst highlighted some key facts: 1) the PERA fund reached a high-water mark of nearly $14 billion in October and has stayed at that approximate level since then; 2) the PERA fund's investment gain for fiscal year (FY) 2013 was 13.26%; 3) recently enacted legislation that reduced the cost-of-living adjustment (COLA) for current and future retirees both reduced the PERA's unfunded liability and, beyond expectations, increased the funded ratio; and 4) all but the volunteer firefighters plan, which is still well funded but which saw a decrease in funding due to a law modestly increasing the benefit, experienced an increase in the funded ratio. Mr. Propst directed the committee's attention to charts showing a 40-year projection of the overall PERA funded ratio, with and without the enactment of pertinent 2013 legislation, and a 40-year projection for each PERA division. He detailed reasons that the PERA board is optimistic, but cautious, in thinking about long-term solvency. Lastly, he presented information on FY 2013 data, including: PERA's obligations; average annual pension amounts and ages at retirement; and payroll by county.

Committee members' questions and comments and Mr. Propst's responses to them are summarized as follows.

- Why is the average retirement age for municipal police and firefighters significantly lower than in the other divisions? Those employees were eligible to retire after 20 years of service. Eligibility for them now begins at 25 years.
- Does PERA intend to support legislation in the next session? Yes, it will support revisions to the judicial and legislative plans. Before making changes to the overall PERA plan, the board will wait to see the impact of 2013 legislation.
- Will the legislative changes to the firefighter plan continue to decrease the funded ratio? Most likely, the ratio will be greater than 100% for the foreseeable future, but the plan's provisions might need to be adjusted to ensure solvency.

- Is the average retirement age expected to increase? Yes.
- Rapid fluctuations in the stock market would seem to put expectations at risk. Mr. Propst responded that analysts use a "smoothing period" to account for losses and gains, but nevertheless, investment insecurity is a reason to exercise caution and to determine whether targeted assumptions are met before requesting a further change in law.
- Should the COLA be tied to a cost-of-living index? The board has concluded that it is better to have a fixed COLA than one that fluctuates.
- How will the Governmental Accounting Standards Board's (GASB's) new reporting requirements change current practices? They will change what may be used as a discount rate for actuarial purposes. Also under the new rules, funding entities will have to report their net pension liability more prominently.
- The recently enacted changes have helped to satisfy a long-standing need.

A member requested that in the future, the map showing payroll by county include the number of retirees in each county.

How Tax Policy Can Be Used to Improve Child Well-Being

James Jimenez, director of policy, research and advocacy integration, New Mexico Voices for Children (VFC), and Bill Jordan, senior policy advisor, governmental relations, VFC, talked about how tax policy affects child well-being in New Mexico. Handouts entitled "Tax Policy & Child Well-Being", "New Mexico State & Local Taxes", "Working Families Tax Credit" and "NM KIDS are COUNTing on Us: A Policy Agenda for a Better New Mexico" were distributed to the committee. In addition, individualized handouts showing how much money is channeled to particular districts by the federal earned income tax credit and the state working families tax credit programs were distributed.

Referring to the first handout, Mr. Jimenez cited reasons for New Mexico's consistent ranking at the bottom of states in child well-being and remarked that some factors contributing to the low ranking are beyond the legislature's control. He said that the presentation would focus on one of four domains related to the ranking — of economic well-being — and the indicators that define it. Income inequality, which he said will always exist but has grown, worsens when government structures reward the highest earners. Mr. Jimenez stressed that the state's tax system is regressive.

Mr. Jordan continued the presentation by citing LFC-identified tax policy principles, noting that "adequacy" and "equity" have the greatest potential, when applied, to improve child well-being. With improved adequacy, more resources are available to fund education, health care and other services that help children. Mr. Jordan commented that the recession caused a scaling back of funding for those types of programs. He asserted that some ways for the state to improve adequacy and equity are to: 1) increase the working families tax credit, which would cost the state about $23 million; 2) repeal the 50% capital gains deduction; 3) impose a 5.9% personal income tax rate on high-income earners; and 4) mandate combined reporting for all corporate filers. VFC further supports the enactment of a tax expenditure reporting requirement to enhance transparency and accountability in the tax system.

Questions and comments from committee members included the following.

- Which taxes are most regressive? Mr. Jimenez indicated that reducing the gross receipts tax rate would most effectively moderate overall tax regressivity.
- All policymakers have the goal of helping the poor; the debate centers on how best to accomplish that goal. Often, proposals intended to increase the burden on the rich and to ease the burden on the poor would, if implemented, invite unintended consequences. The capital gains deduction is an example of a program that, if eliminated, would deter people from selling their businesses in the state and deprive the state of those corresponding tax payments.
- Tax revenues derive from private-sector economic activity, which should be encouraged. Further, the state's tax system is too complicated, and there is too much government regulation. These circumstances deter private-sector economic activity and, thus, dampen potentially robust tax revenues.
- If there were more wealthy people, there would be more tax revenue. With more revenue, there would be more programs to support low-income children.
- A competitive business environment would help children by encouraging job creation.
- This committee is nominated to focus on revenue stabilization, which is synonymous with predictability, reliability and planning. States that have been too progressive in their tax policy have experienced resulting economic downturns. Much of the state population is in the throes of poverty and relies on entitlement benefits, which cost the state heavily. Nevertheless, New Mexico has managed, among other achievements, to avoid a reduction in force of its public employees because it has a broad-based tax policy that is neither too regressive or progressive. The key to this juggling of resources and needs is balance. In the quest for revenue stabilization, revisions to all taxes should be considered.

Status Report of the Proposed Navajo Compact

Ben Shelly, president, Navajo Nation, and LoRenzo Bates, delegate, Navajo Nation Council, addressed the committee. Each spoke from a prepared statement distributed to committee members. Materials related to the Navajo Nation-proposed gaming compact with the state were also distributed to the committee.

Following the formal presentations, committee members asked for clarification on certain points raised by President Shelly and Mr. Bates, including the status of negotiations between the Navajo Nation and the state and on matters that the interim Committee on Compacts will address. The presenters and certain committee members who also serve on the Indian Affairs Committee offered information on developments that were reported to that committee. Derrick Watchman, chief executive officer, Navajo Nation Gaming Enterprise, who was in the audience, addressed the committee in response to some of the questions raised.

Recess

With no further business for the day, the meeting recessed at 4:40 p.m.

<u>Wednesday, December 18</u>

Senator Cisneros reconvened the meeting at 9:16 a.m.

Tax Reform Study

Senator Sharer and Representative Taylor presented to the committee for its consideration a draft bill that would provide funding for experts to conduct a tax reform study. Accompanying their presentation was a handout with a table that outlines many of the state's tax exemptions, deductions and credits. The legislation proposes that experts study and develop recommendations for a tax policy that is simpler and fairer for taxpayers and that makes the state more competitive.

Hold Harmless Gross Receipts Tax and Distribution Changes

Representative Harper, Bill Fulginiti, executive director, New Mexico Municipal League, and Tasia Young, legislation liaison, New Mexico Association of Counties, discussed proposed changes to the hold harmless provisions and provided handouts illustrating aspects of the discussion.

Representative Harper presented for the committee's consideration proposed legislation that would reduce the amounts that local governments can collect from the hold harmless distributions and gross receipts taxes. Mr. Fulginiti presented a draft bill that would adjust the hold harmless distributions to municipalities and counties.

A motion to endorse both bills in concept and with the understanding that work on them would continue was made and seconded. With three members in opposition, the motion passed.

Separate Reporting of Certain Gross Receipts and Compensating Tax Deductions and Exemptions

Representatives Harper and McCamley presented a draft bill for the committee's consideration that would require separate reporting of certain gross receipts and compensating tax exemptions and deductions and sunset procedures for certain of those provisions. A handout showing exceptions to the separate-reporting requirement that are reflected in the bill was distributed to the committee. Senator Keller presented a draft bill that would require separate reporting of certain gross receipts and compensating tax exemptions and deductions. The proposed legislation presented by Representatives Harper and McCamley was endorsed, and Senator Keller's proposed legislation was removed from consideration.

Legislative Proposals: Reporting Requirements; Changes to Working Families Tax Credit and Capital Gains Deduction; and State Graduate Employment Tax Credit

Senator Keller presented a draft joint resolution that would propose a constitutional amendment requiring the annual preparation of a tax expenditure report.

Senator Keller also presented two bills for the committee's consideration: one that would require the TRD to promulgate rules for reporting tax expenditures and one that would increase the working families tax credit and repeal the capital gains deduction. A motion to endorse the first bill was made and seconded. With two members in opposition, the proposed legislation was endorsed by the committee. A motion to endorse the second bill was made and seconded. With six members in opposition, the proposed legislation was endorsed by the committee.

County Government Legislative Proposals

Ms. Young, who was accompanied by Clyde Ward, assessor, San Juan County, and Steve Harris, treasurer, Chaves County, presented two bills for the committee's consideration: one that would address the limitation on increases in valuation of residential property and one that would clarify that a county retains payment of delinquent taxes, penalties and interest for property that is delinquent for two years or less. A motion to endorse the first bill was made and seconded. With three members in opposition, the proposed legislation was endorsed by the committee. A motion to endorse the second bill was made and seconded. With no opposition, the proposed legislation was endorsed by the committee.

Capital Outlay Planning and Monitoring Act

Linda Kehoe, principal analyst, LFC, presented proposed legislation that would increase fiscal and programmatic scrutiny of capital outlay expenditures. Handouts accompanying her presentation — a fiscal impact report and attachments outlining the reasons for and aspects of the legislation — were distributed to the committee. To allow for the legislation to be introduced in both houses, no endorsement was sought.

Endorsement of Legislative Proposals

The committee reviewed for endorsement the following bill drafts.

1. This proposal was removed from consideration.

2. Hold Harmless Gross Receipts Tax and Distribution Changes. ENDORSED, Representative Harper to sponsor.

3. Adjustments to the Hold Harmless Distributions to Municipalities and Counties. ENDORSED.

4. Require Separate Reporting of Certain Gross Receipts and Compensating Tax Exemptions and Deductions; Sunset Certain Gross Receipts and Compensating Tax Exemptions and Deductions. ENDORSED, Representative Harper to sponsor.

5. This proposal was removed from consideration.

6. This proposal was removed from consideration.

7. Require the Taxation and Revenue Department to Promulgate Rules for Reporting Tax Expenditures. ENDORSED, Senator Keller to sponsor.

8. Changes to Working Families Tax Credit and Capital Gains Deduction. ENDORSED, Senator Keller to sponsor.

9. State Graduate Employment Tax Credit. ENDORSED, Senator Keller to sponsor.

10. Changes to the Limitation on Increases in Valuation of Residential Property. ENDORSED, no sponsor identified.

11. Require Affidavits to Be Filed with County Assessors for Real Property Sold in the Counties. ENDORSED, no sponsor identified.

12. Clarify That Payment of Delinquent Taxes, Penalties and Interest for Property That is Delinquent for Two Years or Less Be Retained by the County. ENDORSED, Representative Martinez to sponsor.

13. This proposal was removed from consideration.

14. Determine In-State Sales of Intangibles and Services. ENDORSED, Senator Wirth to sponsor.

15. This proposal was removed from consideration.

16. Require the Valuation of Residential Property at Current and Correct Value for Property That Changes Ownership on or After January 1, 2015. ENDORSED, Representative Egolf to sponsor.

17. Increase the Working Families Tax Credit to 15% of the Federal Earned Income Tax Credit. ENDORSED, Representative Sandoval to sponsor.

18. Deduction for Receipts for Durable Medical Equipment and Medical Supplies. ENDORSED, Representative Jim R. Trujillo to sponsor.

19. This proposal was removed from consideration.

Adjournment

There being no further business, the committee adjourned at 12:45 p.m.